

GASB STATEMENT 34 IMPLEMENTATION ISSUES

Infrastructure Reporting – Modified Approach vs. Depreciation

Issue

To determine the method of reporting to be selected for the reporting requirements for infrastructure assets under GASB Statement 34.

Background

GASB Statement No. 34, paragraph 18 states that capital assets should be reported at historical cost. Paragraph 19 states that capital assets include infrastructure, defined as long-lived capital assets that normally are stationary in nature and normally can be preserved for a significantly greater number of years than most capital assets. Examples given include roads, bridges, tunnels, drainage systems, water and sewer systems, dams, and lighting systems. GASB Statement No. 34 breaks infrastructure assets into networks and sub-systems.

A *network* of assets is a group of assets that provide a particular type of service for a government. An example of a network of infrastructure assets would be a dam composed of a concrete dam, a concrete spillway, and a series of locks.

A *subsystem* of a network of assets is composed of all assets that make up a similar portion or segment of a network of assets. Interstate highways, state highways, and rural roads would each be considered a subsystem of the network of all of the roads of a government.

Buildings, except those that are an ancillary part of a network of infrastructure assets, should not be considered infrastructure assets for purposes of GASB Statement No. 34. Examples of buildings that may be an ancillary part of a network or subsystem include road maintenance structures such as shops and garages associated with a highway system and water pumping buildings associated with water systems.

Discussion of Alternatives

GASB Statement No. 34 gives two alternatives to choose from to account for infrastructure assets. The state must determine which of these two alternatives will be used by all entities that are reported in the CAFR.

(1) *Modified Approach*. The first alternative would be to use the “modified approach”. Under this approach, GASB Statement No. 34, paragraph 23, states that infrastructure assets that are part of a network or a subsystem of a network (described above) are not required to be depreciated as long as two requirements are met.

First, the government manages the eligible infrastructure assets using an asset management system that has the following characteristics:

- (a) the system must have an up-to-date inventory of eligible infrastructure assets
- (b) condition level assessments of the eligible infrastructure assets must be performed and the results must be summarized using a measurement scale
- (c) the annual amount required to maintain and preserve the eligible infrastructure assets at the condition level established must be estimated and disclosed by the government.

Second, the government should document that the eligible infrastructure assets are being preserved approximately at or above a condition level established and disclosed by the government. The amount of documentary evidence sufficient to comply with this requirement is left to professional judgment because of variations among governments' asset management systems and condition assessment methods. However, GASB Statement No. 34, paragraph 24 states that governments should document that:

- (a) Complete condition assessments of eligible infrastructure assets are performed in a consistent manner at least every three years. A government can perform this condition level assessment using statistical samples that are representative of the eligible infrastructure assets being preserved. Also, the condition level assessments can be performed on a cyclical basis. If a government uses this cyclical approach, a condition assessment is considered complete for a network or subsystem only when condition assessments have been performed for all (or statistical samples of) eligible infrastructure assets in that network or subsystem.
- (b) The results of the three most recent complete condition assessments provide reasonable assurance that the eligible infrastructure assets are being preserved approximately at (or above) the condition level established and disclosed by the government.

Under the modified approach, infrastructure assets are required to be capitalized. However, they do not have to be depreciated if the government meets the two requirements discussed above. All expenditures made to maintain these assets under the modified approach would have to be expensed in the period incurred, while expenditures for additions and improvements would have to be capitalized. Per GASB Statement No. 34, paragraph 25, additions or improvements increase the capacity or efficiency of the infrastructure assets rather than preserve the useful life of the assets.

(2) *Depreciation*: The second alternative is to depreciate the capitalized infrastructure assets. Also, if a government no longer meets the requirements for using the Modified Approach, then the infrastructure assets must be depreciated over their estimated useful lives. The depreciation can be calculated for a class of assets, a network of assets, a subsystem of a network, or individual assets. To determine estimated useful lives, a government can use general guidelines obtained from professional or industry

organizations, information for comparable assets of other governments, or internal information.

Discussion of Capitalization Requirements

The capitalization requirements for infrastructure assets applies under either alternative discussed above. GASB Statement No. 34 establishes different capitalization requirements for prospective reporting and retroactive reporting of infrastructure assets. Prospective reporting is required for all *general* infrastructure assets. However, retroactive reporting is only required for *major* infrastructure assets. Determination of a major infrastructure asset should be done at the network or subsystem level and should be based on the following criteria:

- (a) the cost or estimated cost of the *subsystem* is expected to be at least 5 percent of the total cost of all general capital assets reported in the first fiscal year ending after June 15, 1999, or
- (b) the cost or estimated cost of the *network* is expected to be at least 10 percent of the total cost of all general capital assets reported in the first fiscal year ending after June 15, 1999.

The retroactive reporting requirement applies to *major* infrastructure assets acquired, significantly reconstructed, or that received significant improvements in fiscal years ending after June 30, 1980. However, states are not prohibited from choosing an earlier cut off date.

Information Required for Implementation

For prospective reporting, general infrastructure assets must be reported at historical cost. For retroactive reporting of major infrastructure assets, if historical cost is not practical because of inadequate records, estimated historical cost may be used. This may be calculated by determining the current replacement cost of a similar asset and deflating this cost by using price-level indexes to the acquisition year. Existing support documents may contain enough information to derive the estimated historical cost; for example, bond documents, capital project fund expenditures, capital outlay expenditures in governmental funds, and engineering documents. The Department of Transportation and Development (DOTD) may also have other documentation sufficient to determine the estimated historical cost of major infrastructure assets that will be reported retroactively. Meetings with DOTD will provide further guidance on specific information that may already exist or that may be needed.

The current chart of accounts for capital assets will have to be expanded to include infrastructure assets. The infrastructure assets accounts must also have related accumulated depreciation accounts. The accounts will be organized by networks or subsystems of infrastructure assets. The specific number and titles of the accounts will be determined later once the composition of the inventory is established.

Recommendation

We recommend that the state of Louisiana choose the alternative to depreciate the capitalized infrastructure assets. We feel that this is the most cost effective approach for reporting since there would not be any significant burden involved in depreciating the infrastructure assets once they have been identified and capitalized. The schedules of capitalized infrastructure assets would simply include a column to compute the amount of annual depreciation.

Under the modified approach, the capitalization requirements are the same as under the depreciation alternative. However, the cost and effort to follow the requirements of the modified approach would be significant and therefore more of a burden than depreciating the infrastructure assets. In addition, with the uncertainty of state funding to cover the additional costs of maintaining the state's infrastructure at specified condition levels as prescribed in the modified approach, it is possible that the state would have to revert to the depreciation alternative at some point in the future and face a qualification in the year we fail to maintain at the designated level.